

# **VERMONT STATE TEACHERS' RETIREMENT SYSTEM**

Meeting of the Board of Trustees

November 17, 2004

## **Board Members present:**

JOSEPH MACKEY, Chairperson (Active No. 29334), term expiring July 1, 2005

JON HARRIS, Vice-Chairperson (Active No. 25669), term expiring July 1, 2007

JAY KAPLAN, Association of Retired Teachers of Vermont, term expiring July 1, 2008

THOMAS CANDON, representing Commissioner of BISHCA

VAUGHN ALTEMUS, representing Commissioner of Education

JEB SPAULDING, VT State Treasurer

## **Also attending:**

Cynthia Webster, Director of Retirement Operations

David Minot, Director of Investment Services

Elizabeth Pearce, Deputy Vermont State Treasurer

Dick Charlton, Ellen Griggs, Kevin Kondry, NEPC

William Griffin, Chief Assistant Attorney General

Angelo Dorta, VT-NEA

Dave Grundy, Association of Retired Teachers of Vermont

Michael Sweatman and Jo Bradley, VETA/VOF

Investment Manager personnel

The Chairperson, Joe Mackey, called the meeting to order at 8:09 a.m. on Wednesday, November 17, 2004, at the Hilltop Inn Conference Room, Airport Road, Berlin, Vermont.

## **ITEM 1:      Approval of the Minutes of October 25, 2004**

**On a motion by Mr. Altemus seconded by Mr. Kaplan, the Board unanimously voted to approve the minutes of October 25, 2004, as submitted.**

## **ITEM 2:      Approve the Disability Retirement for: Linda VanBallenberghe**

**At 8:12 a.m. on a motion by Mr. Candon seconded by Mr. Kaplan, the Board unanimously voted to enter into executive session, pursuant to Title 1 §313 to discuss medical information.**

At 8:19 a.m. the Board moved out of executive session.

**On a motion by Mr. Kaplan seconded by Mr. Candon, the Board unanimously voted to approve the disability retirement for Linda VanBallenberghe, as recommended by the Medical Review Board.**

## **ITEM 3:      Investment Consultant Report for Q2/04**

Mr. Charlton, Ms. Griggs and Mr. Kondry reviewed the third quarter 2004 performance. They reported the market value of the fund balance at approximately \$1.235 billion and a gross quarterly return of 0.4%, an out performance of the 0.3% median public fund. The one-year return was 12.8% vs. the median public fund at 11.5%, three-year return 7.7% vs. the median public fund at 6.8% and a five-year return of 5.1% vs. 4.6%.

**On a motion by Mr. Spaulding seconded by Mr. Altemus, the Board unanimously voted to authorize NEPC to initiate an RFP for an international growth manager to replace SSgA/Putnam Investments, and at the time of finalist presentations SSgA will also be invited to explain the value of an index product.**

With the Board's permission, items on the agenda were now taken out of order.

**ITEM 4: Ratify Travel Request – AFL-CIO Office of Investment Conference  
Jay Kaplan, September 28 & 29, 2004, Boston, MA**

**On a motion by Mr. Altemus seconded by Mr. Mackey, the Board unanimously voted to ratify the prior ballot vote to grant permission to Jay Kaplan to attend the AFL-CIO Office of Investment Conference, September 28 & 29, 2004, Boston, MA.**

Mr. Kaplan will provide a presentation on information gleaned from this conference, to the Board at the February meeting.

**ITEM 5: Director of Finance & Investments Report**

▪ **Securities Lending**

Mr. Minot distributed an October 2004 State Street Bank securities lending report for Board discussion. The report for the most recent 10-month period showed \$114,446.38 earned. Mr. Minot was asked to research the potential impact to security lending income and/or fees for separately or commingled indexed accounts.

▪ **SPIF/STIF Investment Policy**

Mr. Minot reported that at 10:00 a.m. each day, State Street Bank sweeps 80% of equity managers cash balances into a SPIF and the remaining 20% into a STIF, pursuant to a contractual agreement signed by the previous Investment Director. Upon review of the agreement letter, Mr. Minot was requested to clarify whether 100% should be swept to the SPIF, and not split.

Mr. Minot also noted he was comfortable that the guidelines described under the "derivatives policy" in the Board's *Investment Guidelines*, addressed SPIF and STIF.

**ITEM 6: Investment Manager Presentations**

**Loomis Sayles:** Peter Palfrey, Portfolio Manager, and Timothy Haarmann, VP Client Product Manager, appeared before the Board. The domestic fixed income portfolio was reported to have a market value of approximately \$151.4 million with a Q3/04 return of 3.1% compared to the Lehman Brothers Aggregate Index of 3.2%, one-year return was 4.5%, three-year return 5.4% and five-year return 7.2%.

The Board discussed the value of active fixed income management of the funds vs. an indexing product with the manager.

The manager was requested to provide the Board with recommendations for a redesigned portfolio, which should include guidelines, fees, benchmark, and risks for the new model.

**UBS Realty Investors:** Ann Dakille, Assistant Portfolio Manager, appeared before the Board. The actively managed, open ended, commingled, core portfolio of equity real estate was reported to have 117 investments and \$5.7 billion in assets of which approximately \$42.3 million of the market value is from the VSERS. The Q3/04 return was 4.0% compared to the NCREIF Index of 3.4%, one-year return was 12.7%, three-year return 9.4% and five-year return 10.2%.

Ms. Dakille advised the Board of the recent retirement of Dan Leary.

**Fidelity Investments:** Anthony Dell, Vice President, Relationship Manager and Joe Day, Vice President, Co-Portfolio manager appeared before the Board. The large cap growth portfolio was reported to have a market value of approximately \$143.4 million with a Q3/04 return of (4.5)% compared to the Russell 1000 Growth Index of (5.2)%, one-year return was 8.0%, three-year return 2.2% and five-year return (3.1)%.

The manager was advised of the Board's intention to move to an indexing strategy, in the near future.

#### **ITEM 7: Treasurer's Report**

- **Consideration of Environmental Investment Proposal**

Mr. Spaulding reviewed the August 2004 proposal memo, summarized his opinions, and queried the Board on their interest in directing NEPC to initiate an RFP for investment in environmentally managed funds from the large cap mandate.

**On a motion by Mr. Spaulding seconded by Mr. Altemus, the Board voted to consider an allocation to an environmentally sound investment strategy, and direct NEPC to conduct an RFP for an environmentally managed US large cap mandate as described in the August 2004 memo. Mr. Spaulding, Mr. Altemus, Mr. Harris voted yes. Mr. Kaplan, Mr. Mackey, Mr. Candon voted no. Motion failed.**

Mr. Candon indicated he would reconsider at a later date, once other pending Board issues were resolved.

- **Proxy Voting Report**

Mr. Spaulding and Mr. Minot reviewed the November 8, 2004, Vermont Retirement Systems' Institutional Shareholder Investor proxy voting report for Q1&Q2 2004. Reported were votes in the areas of Director Elections, Compensation, Auditor Ratification, and Capital Structure.

Mr. Minot advised the Board he would follow-up with ISS and the money managers regarding report format, discrepancies, policy guidelines, etc. Mr. Minot will also research the impact to proxy voting with a transition to indexed funds.

Mr. Minot will e-mail the report to Board members.

- **VEDA/VOF Overview**

Michael Sweatman and Joe Bradley provided an overview of a new investment plan initiative for the Board's future consideration.

- **Discuss Pension Investments that Support Terrorism**

Mr. Spaulding explained the request was made by Frank J. Gaffney to discuss specific retirement fund investments with alleged entities associated with the sponsorship of terrorism.

The Board thanked Mr. Spaulding for sharing the information and agreed they look forward to seeing a federal or SEC guideline, policy, or list of terrorism sponsoring companies, when developed.

- **Shareholder Resolutions**

The Treasurer advised the Board, pursuant to their prior approval, he had joined AFSCME and several other states in co-sponsoring shareholder resolutions at Lily, Wyeth, and Pfizer regarding their actions relating to prescription drug re-importation.

- **Unitization**

Mr. Spaulding advised the Board it was his hope to bring people together to continue working towards a unitization proposal.

The Board reiterated its continued support, in concept, of unitization and would support moving forward and would also like to be involved in final discussions regarding Investment Board composition.

## **ITEM 8:     Director of Retirement Operations Report**

- **FY'06 Budget Recommendations**

Ms. Pearce reviewed the 6/30/04 balance sheet and income statement provided in the November 9, 2004 draft, and also provided an update on the status of the retirement administration-reengineering project.

The Board requested Ms. Pearce prepare a comprehensive and detailed breakdown of the system's income and expenses.

Mr. Kaplan also asked for a comparison of the current office staff expenses under the prior administration vs. the current administration, including staff changes/additions, etc.

By consensus the Board accepted the preliminary budget presentation. Comments, if any, should be referred directly to Ms. Pearce.

▪ **Legislative Initiatives**

Ms. Webster explained that annually several issues come before the Legislature that are never resolved, i.e. retired teacher's subsidy for spousal health coverage. As a result the Treasurer was directed by the legislature to conduct a summer study committee to discuss and collectively resolve several outstanding retirement statute issues. Several meetings with a wide representation of stakeholders have been held.

Mr. Kaplan expressed his concern that meetings were being held to discuss retirement policy and issues that could effect retired teachers without the Board being notified first. The Treasurer acknowledged his concern but informed the Board as part of nearly 15 participants, VT-NEA, the VSTRS Chair, and both an active and retired teacher who are legislators, are taking part in discussions. He assured Mr. Kaplan that retiree interests were being considered. Further the Board was advised that any of committee's proposals would be brought to the Board before formal recommendations are offered.

Ms. Webster distributed copies and of draft legislative amendments to the disability statutes, 16 V.S.A §1938, §1938a, and a proposed definition of "gainful occupation" and "other income".

Mr. Spaulding reviewed the 10/27/04 summary of the 2004 Summer Retirement Study Advisory Committee items discussed regarding health care coverage. He said the items considered were for new teachers - prospectively, unless proven acceptable to also be included in the current membership. Proposals, if implemented, would represent a decrease in the system's liability.

Mr. Mackey said he felt no discussion or changes to the health care plan benefit should be considered while the system is so grossly under funded. Mr. Kaplan asked the Treasurer to verify whether the actuary's information provided to the Summer Committee regarding funding included grandfathering of current members.

Mr. Mackey said he did not support any type of means testing, and suggested any other comments should be referred to Mr. Spaulding, Ms. Webster, or Mr. Mackey.

***Mr. Kaplan and Mr. Mackey left the meeting. Mr. Harris assumed the role as Chairman.***

**ITEM 9: Recommendation Regarding Professional Leave Compensation**

Mr. Harris provided background information regarding this query. The Board reviewed a copy of Ms. Webster's written recommendation, requested by the Board for consideration.

Mr. Griffin said he supported the recommendation.

**On a motion by Mr. Altemus seconded by Mr. Candon, the Board unanimously voted to adopt the Director of Retirement Operation's recommendation that compensation paid for an approved leave for professional development be included in a member's total retirement reportable earnings.**

Mr. Harris will discuss reporting requirements with Ms. Webster.

**ITEM 8: Director of Retirement Operations Report (CONTINUED)**

▪ **Fitzgerald Recommendation**

A copy of Ms. Webster's written recommendation, requested by the Board for consideration was reviewed. Mrs. Webster noted she discussed the recommendation with Mr. McShane who is completely comfortable with the recommendations. The Board agreed she should not recuse herself from further administration of the issue.

**On a motion by Mr. Spaulding seconded by Mr. Altemus, the Board unanimously voted to approve the Director of Retirement Operation's recommendation to deny Mr. Fitzgerald's request to be allowed to pay back only the amount that he received under the Level Income Plan prior to his return to active teaching service in 1995, and support the Director of Retirement Operation's administrative actions previously taken in this matter.**

**ITEM 10: Any other business to come before the Board**

Mr. Candon asked for clarification of the process and expectations for the December 9<sup>th</sup> meeting.

Mr. Harris suggested an agenda item to discuss strategies moving forward.

Mr. Altemus asked if the Board should be discussing the expected rate of return with the Actuary. Also questioned was whether the Board should be discussing the accepted actuarial valuation and the continued impact of raising expenses and under funding.

**Next Meeting Dates:**

The next scheduled meeting of the Board is December 9, 2004.

The next quarterly investment meeting is scheduled for February 16, 2005.

**On a motion by Mr. Spaulding seconded by Mr. Candon, the Board unanimously voted to adjourn at 2:50 p.m.**

Respectfully submitted,

Cynthia Webster  
Secretary to the Board